

Raw materials that will be incorporated into manufactured goods and resold may be purchased free of tax as purchases made for the purpose of resale. See 86 Ill. Adm. Code 130.1405(b). (This is a GIL).

February 24, 1999

Dear Mr. Xxxxx:

This letter is in response to your letter dated January 28, 1999. The nature of your letter and the information you have provided require that we respond with a General Information Letter, which is designed to provide general information, is not a statement of Department policy and is not binding on the Department. See 86 Ill. Adm. Code 1200.120(b) and (c), enclosed.

In your letter, you have stated and made inquiry as follows:

I am writing to seek legal guidance with regard to the Illinois tax obligations of a company, Corporation X. X, which maintains no regular place of business outside New Jersey and is engaged in the manufacture of components. The ultimate purchaser of the components incorporates them into the manufacture of equipment. With regard to X's sales to Illinois destinations, to date, X has sold its components exclusively to independent distributors.

In other states, X sells its products predominantly for resale to independent distributors, but on an isolated basis in states other than Illinois, X has made sales of components to unrelated manufacturers. It is my understanding that in those isolated transactions outside Illinois, the manufacturer could properly have avoided state sales tax by providing X with an exemption certificate, but that X was unaware of any need to secure such certificates from its manufacturing customers in such transactions.

In Illinois and throughout the United States, X solicits sales of its products through the services of independent sales representatives (reps) which do not work exclusively for X, but, rather, represent other unrelated manufacturers, as well as X. For more than ten years, X has employed an Illinois resident individual ('A') to provide sales support and guidance to a number of its reps. X has treated individual A as an employee, has been registered for Illinois personal income-tax withholding and has withheld and remitted all appropriate taxes to Illinois, as well as unemployment and disability taxes, but has not registered with Illinois for sales and use tax, or any other business tax purpose.

X has requested resale certificates from all of its Illinois distributors. Based on a conversation with PERSON on January 15, we were advised, but wish to seek written confirmation, that X is

obligated to register as a re-seller and to submit Form NUC-1. I was further advised that Illinois does not impose penalties for X's inadvertent failure to submit Form NUC-1 when it first had sales and use-tax nexus in Illinois, and that, furthermore, upon submitting Form NUC-1, so long as all of X's Illinois-destination sales are for resale, X is not obligated to file any Illinois sales tax return. Would you kindly confirm such advice.

Finally, X's distributors in Illinois and other states occasionally cause X to engage in drop-shipments wherein X's components are billed to the distributor and shipped directly to the distributor's customers. In light of the fact that X bills all of its drop-shipment transactions to its distributor customers in resale transactions, could you kindly provide guidance on Illinois' position on drop-shipment transactions under two alternatives:

- 1) When X's customer has nexus in Illinois and can provide X with the required Illinois resale certificate; or
- 2) When drop-shipments made to Illinois recipients are billed to non-Illinois distributors which cannot provide X with an Illinois resale certificate.

Finally, if in the future X engages in a sale of its components directly to an Illinois manufacturer for incorporation into that buyer's manufactured products, I understand that such a transaction would simply be regarded as a resale transaction. Would you confirm whether such a resale transaction would change X's reporting requirements to Illinois? Please understand that on the basis of X's experience in other states, if such a transaction were to occur with an Illinois manufacturer, it would likely be isolated, rather than recurring.

Thank you in advance for your response to this inquiry. My client and I would appreciate your incorporating into the response the statutory, regulatory or other policy authority for Illinois's position and providing me with any necessary forms which X is required to file.

Resale numbers are issued to persons who make no taxable sales in Illinois but who need the wherewithal to provide suppliers with Certificates of Resale when purchasing items that will be resold. So long as those persons make no taxable sales in Illinois, those persons can qualify for a resale number which does not require the filing of tax returns with the Illinois Department of Revenue. Persons applying for a resale number should complete an Illinois Business Registration (NUC-1) form. See enclosed copy of the NUC-1. There is no specific amount of sales for resale required for persons to obtain resale numbers. The only qualification is that those persons make no taxable sales in Illinois. Persons that obtain resale numbers and no longer intend to make any sales for resale should notify the Department so that their resale numbers can be cancelled.

A drop-shipment situation is one in which out-of-State purchasers (Purchasers) make purchases for resale from companies (Companies) which are registered with Illinois and have those Companies drop-ship the property to Purchasers' customers (Customers) located in Illinois. For this discussion, it

is assumed that Purchasers are out-of-State companies that are not registered with the State of Illinois and do not have sufficient nexus with Illinois to require them to collect Illinois Use Tax.

As sellers required to collect Illinois tax, Companies must either charge tax or document exemptions when they make deliveries in Illinois. In order to document the fact that their sales to Purchasers are sales for resale, Companies are obligated by Illinois to obtain valid Certificates of Resale from Purchasers. See the enclosed copy of 86 Ill. Adm. Code 130.1405. Certificates of Resale must contain the following items of information.

1. A statement from the purchaser that items are being purchased for resale;
2. Seller's name and address;
3. Purchaser's name and address;
4. A description of the items being purchased for resale;
5. Purchaser's signature and date of signing;
6. Purchaser's registration number with the Illinois Department of Revenue; purchaser's resale number issued by the Illinois Department of Revenue; or, a statement that the purchaser is an out-of-State purchaser who will sell only to purchasers located outside the State of Illinois.

If Purchasers have no nexus with Illinois, it is unlikely that Purchasers would be registered with Illinois. If that is the case, and if Purchasers have no contact with Illinois which would require them to be registered as out-of-State Use Tax collectors for Illinois, then Purchasers could obtain resale numbers which would provide them the wherewithal to supply required numbers to Companies in conjunction with Certificates of Resale. We hope the following descriptions of out-of-State sellers required to register, either as Illinois retailers or as out-of-State Use Tax collectors and persons who qualify for resale numbers will be useful.

Assuming a delivery in Illinois, Illinois retailers are anyone who either accepts purchase orders in Illinois or who sells items of tangible personal property which are located in Illinois at the time of sale. See the enclosed copy of 86 Ill. Adm. Code 130.605(a).

Out-of-State sellers who fall under the definition of a "retailer maintaining a place of business in this State" (see 86 Ill. Adm. Code 150.201(i), enclosed) must register to collect Illinois Use Tax from Illinois customers and remit that tax to the Department. See 86 Ill. Adm. Code 150.801(c), enclosed. Please note that out-of-State sellers with any kind of agent in Illinois (not just sales or lease agents) are required to register as out-of-State Use Tax collectors. If Company B has no contact with Illinois, it does not fall within the definition of a "retailer maintaining a place of business in this State," and it need not register as an out-of-State Use Tax collector.

The United States Supreme Court in *Quill Corp. v. North Dakota*, 112 S.Ct. 1904 (1992), set forth the current guidelines for determining what nexus

requirements must be met before a person is properly subject to a state's sales tax laws. The Supreme Court has set out a two-prong test for nexus. The first prong is whether the Due Process Clause is satisfied. Due Process will be satisfied if the person or entity purposely avails himself or itself of the benefits of an economic market in a forum state. Id. at 1910. The second prong of the Supreme Court's nexus test requires that, if due process requirements have been satisfied, the person or entity must have physical presence in the forum state to satisfy the Commerce Clause.

A physical presence does not mean simply an office or other physical building. Under Illinois tax law, it also includes the presence of any representative or other agent of the seller. The representative need not be a sales representative and it is immaterial for tax purposes that the representative's presence is temporary.

As stated above, resale numbers are issued to persons who make no taxable sales in Illinois but who need the wherewithal to provide suppliers with Certificates of Resale when purchasing items that will be resold. So long as Purchasers do not act as Illinois retailers and, so long as they do not fall under the definition of a "retailer maintaining a place of business in this State", their sales to Illinois customers are not subject to Illinois Retailers' Occupation Tax liability and they cannot be required to act as Use Tax collectors. So long as this is true, Purchasers qualify for resale numbers that do not require the filing of tax returns with the Illinois Department of Revenue. See 86 Ill. Adm. Code 130.1415.

Please note that the fact that Purchasers may not be required to act as Use Tax collectors for Illinois does not relieve their Customers of Use Tax liability. Therefore, if Purchasers do not collect Illinois Use Tax from their Customers, the Customers would have to pay their tax liability directly to the Illinois Department of Revenue.

While active registration or resale numbers on Certificates of Resale are still preferred, the Illinois Retailers' Occupation Tax Act provides as follows:

"Failure to present an active registration number or resale number and a certification to the seller that a sale is for resale creates a presumption that a sale is not for resale. This presumption may be rebutted by other evidence that all of the seller's sales are sales for resale or that a particular sale is a sale for resale." 35 ILCS 120/2c.

Again, including registration or resale numbers from Purchasers on Certificates of Resale is the preferred method for documenting that their purchases from Companies are purchases for resale. However, in light of this statutory language, certifications from Purchasers on Certificates of Resale in lieu of resale numbers which described the drop-shipment situation and the fact that Purchasers have no contact with Illinois which would require them to be registered and that they chooses not to obtain Illinois resale numbers would constitute evidence that this particular sale is a sale for resale despite the fact that no registration number or resale number is provided. The risk run by Companies in accepting such a certification and the risk run by Purchasers in providing such a certification is that an Illinois auditor is much more likely to go behind a Certificate of Resale which does not contain a valid resale number and require that more information be provided by Companies as evidence that the

particular sale was, in fact, a sale for resale.

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I hope this information is helpful. The Department of Revenue maintains a Web site, which can be accessed at www.revenue.state.il.us. If you have further questions related to the Illinois sales tax laws, please contact the Department's Taxpayer Information Division at (217) 782-3336.

If you are not under audit and you wish to obtain a binding Private Letter Ruling regarding your factual situation, please submit all of the information set out in items 1 through 8 of the enclosed copy of Section 1200.110(b).

Very truly yours,

Melanie A. Jarvis
Associate Counsel

MAJ:msk
Enc.